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Top Secret 217

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NATIONAL INTELLIGENCE DAILY CABLE

Saturday June 11, 1977

CG NIDC 77-135C

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NATIONAL SECURITY INFORMATION
Unauthorized Disclosure Subject to Criminal Sanctions

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National Intelligence Daily Cable for Saturday, June 11, 1977.

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The NID Cable is for the purpose of informing senior US officials.

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ITALY: Interparty Political Talks

25X1 [] Hard bargaining marked this week's bilateral talks by Italy's ruling Christian Democrats with the Communists and with the four other parties that abstain in parliament and thereby keep the government of Prime Minister Andreotti in office. The talks, which are being held mainly in response to Communist pressure for a more direct role in government policy-making, were to have entered a final phase this week with a series of roundtable conferences involving the six party leaders. No dates have been set for these meetings, however, because of continuing interparty differences that came to light in negotiations at the technical level late last week.

25X1 [] The Communists in particular are anxious to switch to the roundtable format because it would graphically emphasize the political significance of a program agreement in which the party is formally included. The Communists, however, now appear to be bargaining more aggressively, and new difficulties have arisen, even in areas where the Communists and Christian Democrats seemed close to agreement last week.

25X1 [] For example, while the Communists remain favorably disposed to the tougher law-and-order measures proposed by the Christian Democrats, the two parties are having difficulty resolving differences on the most sensitive questions, such as whether to grant police the power of preventive detention.

25X1 [] The negotiations are also complicated by the Socialists' tendency to take a more strident line than the Communists--a tactic that makes it more difficult for the Communists to compromise with the Christian Democrats. Both leftist parties are putting renewed stress on the need for some political "guarantee" that an agreed program would actually be implemented, but the Socialists' demands go much further than those of the Communists.

25X1 [] The Communists would evidently be satisfied with a relatively minor symbolic step and are again raising the possibility of including in the cabinet a few technocrats considered sympathetic to the left. But the Socialists are asking for the formation of a new government, which--even if it did not differ in composition from the present one--would formally

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include the Communists in its parliamentary majority. The Christian Democrats have consistently refused to go that far, and the Communists themselves appear to consider the proposal unrealistic in present circumstances.

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[] Complex motives are behind the Socialists' militant posture, but in general it reflects the party's desire to prevent the Communists from being the sole spokesmen for the left in the negotiations with the Christian Democrats. The Socialists are seeking also to ensure that the Communists are unable to avoid responsibility for government actions. Finally, the Socialists hope to capitalize on the discontent of some Communist supporters over the party's tendency to cooperate with the government.

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[] The Christian Democrats, meanwhile, seem increasingly concerned with the problem of minimizing the political implications of a formal program agreement involving the Communists. Throughout the talks, the Christian Democrats have sought to keep the discussion of substantive issues separate from speculation about future political formulas, but increasing pressure from the left is making it difficult to maintain the distinction.

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[] The party, moreover, seems divided over how to respond to the left's demands. Some Christian Democrats, such as Andreotti, are open to the idea of a cabinet shuffle bringing in more technocrats. Other leaders, such as party president Moro, regard such a move as politically dangerous, because a parliamentary confidence vote might be required if the changes are extensive.

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[] Thus, no clear end is in sight for the negotiations, which have preoccupied Italian party leaders since late April. Andreotti hopes that an agreement can be reached within the next two to three weeks--enabling his government to survive at least until the fall--but others in the party suggest that the talks could drag on into July. []

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CANADA-JAPAN: Vancouver Meeting

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[redacted] //Canadian Foreign Minister Jamieson and Japanese Foreign Minister Hatoyama will discuss a wide range of economic and political issues during their talks on Monday and Tuesday in Vancouver, British Columbia. This will be the first meeting of the Canada-Japan Joint Economic Committee established last October. Although the conference ostensibly will focus on economic matters, the major issue is certain to be Canada's insistence that Japan accept tough nuclear safeguards in return for a resumption of uranium shipments.//

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[redacted] //The "Framework for Economic Cooperation" signed last year in Tokyo by Prime Minister Trudeau reflects Trudeau's effort to foster economic and political ties with nations other than the US--the so-called "third option."//

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[redacted] //The accord is similar to the "contractual link" Canada signed earlier last year with the EC, and has as its goal expanding the \$4 billion worth of annual trade between the two countries by increasing exports of Canadian-manufactured goods. Neither agreement, however, has provided the boost in economic relations sought by Ottawa, largely because Japan and the EC are more interested in Canadian raw materials than industrial products.//

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[redacted] //At Vancouver, the Canadians will be pressing for increased Japanese investment in energy-related fields, such as the development of coal deposits in British Columbia and oil extraction technology for the tar sands in Alberta.//

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[] //The Japanese can be expected to seek assurances of continued access to raw material supplies, particularly minerals, and to lobby for less restrictive government controls over foreign investment. Japanese businessmen have long argued that Canadian limitations on foreign ownership strongly discourage investment from abroad.//

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[] //The hard bargaining, however, is certain to be over nuclear safeguards and uranium shipments. The Canadians suspended uranium shipments to Japan in January because of Tokyo's refusal to go along with Ottawa's insistence on maintaining control over the transfer of nuclear materials and subsequently developed nuclear-related technology to third countries. The two countries apparently were near agreement when the Canadians added the caveat that their safeguards would apply even to Canadian uranium sold to Japan and undergoing enrichment in the US.//

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[] //Foreign Minister Jamieson has implied that Ottawa may be prepared to back off somewhat from the latter condition. He indicated on Thursday that Canada and Japan should be able to work out their differences at the talks next week. The Japanese apparently had earlier hinted that Hatoyama might not attend the Vancouver talks in light of the breakdown of the nuclear negotiations unless the Canadians were willing to give ground.//

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[] //Canadian officials in both government and private sectors of the nuclear industry are pressing the government to give greater consideration to economic and energy factors in shaping nuclear export policies. []

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USSR-US: Cut in Western Trade

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The USSR is planning an overall cut in trade with the West this year and next because of a severe trade deficit with the US and other countries. US officials learned of the plan at a meeting of the joint US-USSR Commercial Commission, which ended yesterday in Washington. Soviet officials said the cuts would affect both agricultural and non-agricultural products and indicated that they would apply to all Western trading partners. The Soviets gave no indication that it was in any way directed against the US.

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Last year, Moscow's hard-currency trade deficit with Western countries was \$4.9 billion; trade with the US accounted

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for nearly half of the deficit, according to Soviet statistics. Grain imports valued at an estimated \$3 billion--half from the US--were a leading factor in the deficit. The grain imports were necessary because of the poor Soviet harvest in 1975.

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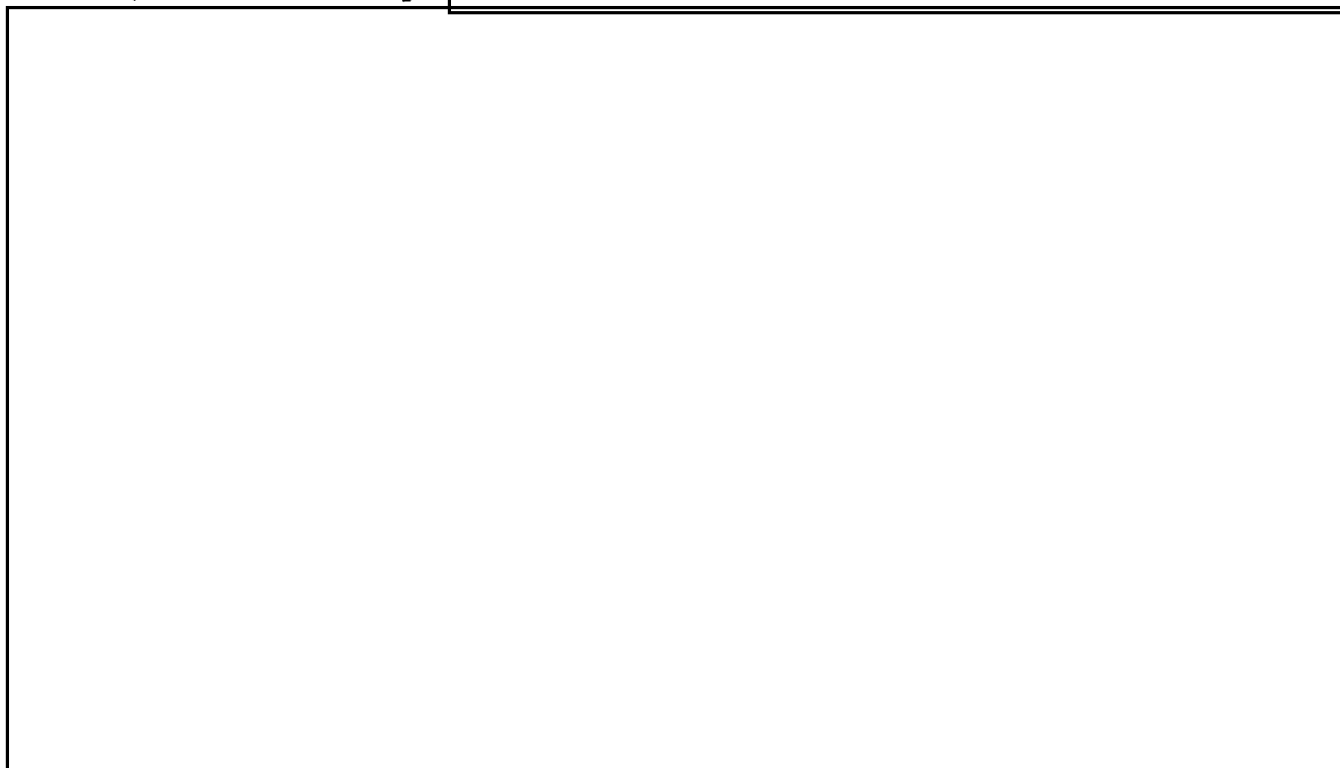
[] Last year's record harvest allows Moscow to reduce the cost of its grain imports this year by an estimated \$2 billion; early indications for another good harvest this year suggest that Moscow may be able to keep its grain imports at minimum levels next year as well. These imports will largely reflect the USSR's commitment to purchase 6 million tons of grain from the US, worth roughly \$700 million, per year through 1980. A Soviet grain delegation in Washington last month would only say that Moscow would meet the minimum requirement in purchasing grain from the US this year.

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[] So far, there is no sign that a trade cutback has begun. Soviet statistics for the first quarter of this year show a 5.4-percent increase in total trade with hard-currency Western countries. Soviet orders for Western plant and equipment, moreover, remain strong. []

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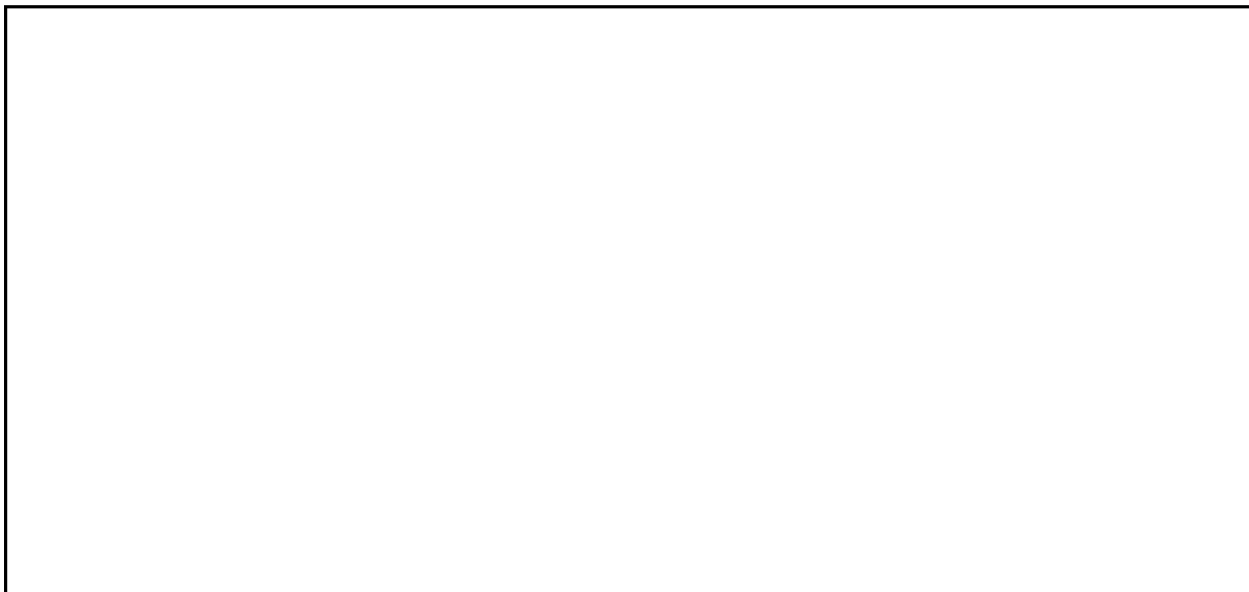
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UNITED ARAB EMIRATES: Bank Crisis

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[REDACTED] //A banking crisis in the United Arab Emirates has led the government to close two banks and impose controls on credit expansion. To avoid recurring crises, the individual emirates will have to cede enough power to the federal government to give it effective control over the banking sector.//

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[REDACTED] //The UAE has tried in the past two years to establish itself as a financial center. To encourage local banking operations, the government has avoided tight controls on the banks. The UAE's Currency Board oversees banking activities.//

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[REDACTED] //The number of banks in the UAE has risen sharply because of the loose controls and high-yielding credit opportunities afforded by the area's booming economy. Many banks are undercapitalized and have become involved in speculative ventures; interbank lending has often been used to create needed reserves.//

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[REDACTED] The government has become increasingly alarmed at such unsound banking practices; in late May it forced two banks that had severely overcommitted their resources to close by canceling their clearing privileges.

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[] //UAE President Zayid has reacted to the banking problems by implementing some long-awaited policy measures to slow credit expansion and to force banks to operate on a sound basis. The government has banned the establishment of any new financial institutions, raised the reserve requirement from 5 percent to 7.5 percent, required a ratio of no less than 1 to 15 of a bank's capital and reserves to total liabilities, and brought all financial institutions under the control of the Currency Board.//

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[] //These regulations will help solve the immediate banking crisis and will hamper some of the free-wheeling tactics of the local banks. The controls on credit expansion, however, have already caused a down turn in the local building industry and could adversely affect other sectors of the economy as well.//

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[] //The new banking regulations still leave most local banks with a competitive edge over branches of foreign-based financial institutions. Many of the local banks, however, may have to merge to achieve a larger capital base.//

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CHILE: Economic Situation for 1977

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[] *Gradually recovering world copper prices and rising noncopper exports should permit Chile some relief from the harsh fiscal and monetary measures of recent years. The ruling military junta plans a 24-percent increase in imports this year. The gain will spur a recovery in real gross national product from the severely depressed 1975-76 levels and should further aid in reducing Chile's triple-digit inflation.*

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[] Unlike most countries of comparable development and sophistication, Chile had to slash imports--and thus domestic income and employment--to cope with the payments problems stemming from rising oil prices and world recession. Until recently, its extremely weak international credit rating practically ruled out access to commercial funds. World criticism of Chilean human rights practices severely limited new official economic assistance and made foreign debt renegotiation difficult at best.

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[] The Chilean populace has complained little about the austerity because of the threat of government repression and, more importantly, because many citizens--if not most--still feel they are better off than under the Allende regime.

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[] The balance of payments had improved considerably by mid-1976 because of rising earnings from noncopper exports, booming copper production, moderate recovery in world copper prices, and short-term capital inflows attracted by soaring interest rates. The junta took advantage of the improvement to terminate its foreign debt renegotiation efforts and to rebuild foreign reserves. Although peso devaluation was slowed and tariffs were further cut, other fiscal and monetary measures caused imports for the year as a whole to drop an additional 8 percent.

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[] This year the military government intends to use its improved foreign reserve position and the small additional gain expected in export earnings to permit an increase in imports sufficient to restore real gross national product to the 1974 level. Although this will require some easing of austerity, the government hopes that increased supply will permit continued progress against inflation. It also intends to avoid debt renegotiations and to assert its independence of the US and other critics of its human rights practices by sharply reducing borrowing from governments and international agencies.

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[] Exports are likely to rise about 7 percent in 1977, to \$2.1 billion. Copper shipments will remain roughly at last year's level of 980,000 tons, but an expected rise in average copper prices will boost earnings moderately. Stronger demand for noncopper exports in markets developed since 1973 should allow sales of such goods to rise to \$820 million, despite an expected weakening in Chile's competitive position because of slower peso devaluation.

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[] The government's reduction of US and International Monetary Fund aid this year will lead to a cut in official capital inflows to around \$180 million, compared with \$460 million in 1976. Chilean missions to the US and Western Europe are seeking commercial bank loans to help fill the gap.

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[] Direct investment will remain low, mainly because of past bureaucratic delays in approving new projects. Full debt amortization payments for 1977 will require \$555 million, slightly more than in 1976. Total net capital inflows will consequently shrink to about \$170 million, compared with \$680 million in 1976.

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[] Chile is expected to increase imports to about \$2 billion. Higher domestic wheat yields and low wheat import prices will permit a reduction in spending for food imports. Most of the increase in imports will come in fuels, raw materials, and goods for industry. Bringing total imports to the target level will require about \$175 million more than Chile now expects to receive from trade and capital flows. Given the recent improvement in the Chilean credit rating, we believe that Chile can raise this additional amount from private sources.

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[] Although the junta is still pursuing a strong anti-inflation policy, it intends to ease austerity. Real wages are to be increased about 5 percent. The junta began a slight relaxation of its restrictive monetary policy in the first quarter. It announced a moderate program of tax reductions, increased social spending, and wage increases for government workers on May 1. These steps are expected to result in a government deficit of around 12 percent of expenditures this year--well below the 17-percent deficit of 1976.

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[] Growth in the money supply is expected to decline from last year. The attack on inflation was also aided by a two-month voluntary price freeze by private industry that ended in May. On balance, we estimate that inflation will decline in 1977.

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[] With somewhat stronger demand, real gross domestic product should grow 6.5 to 7 percent this year. Finished

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goods inventories in some industries are likely to hold industrial growth to 10 percent, compared with 12.2 percent last year. Good weather should permit agricultural production to rise as much as 7 percent above last year. Construction activity, which began picking up late last year, should grow this year for the first time since 1974. Employment will rise some 4.5 percent this year. The unemployment rate will decline only slightly, to 12.2 percent.

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